HARGREAVES
LANSDOWN

THE RULES OF ENGAGEMENT >

This paper explains how to help pension members transition from disengagement to engagement.

A policy paper from Hargreaves Lansdown, it's not designed for individual investors.
September 2018

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EXECUTIVE SUMMARY

Auto-enrolment and pension freedoms are widely recognised as having transformed the UK's pension system for the better.

However, they're based on incompatible underlying approaches; one uses inertia to create good outcomes for individuals without the need for them to take any action, the other is built around giving the same individuals the freedom to choose how and when they access their retirement savings.

Auto-enrolment gives employees the opportunity to save in a pension without thinking about it. This is a good thing. Minimising barriers to just being involved is great, but the system is not perfect.

By the time they want to access their pension, they need to be comfortable making decisions about how and when they'll do it. These choices are vitally important to understand, as what they do makes a huge difference to the value they enjoy from their retirement savings.

As well as this, the decisions they take along the way, as they save through their 20s, 30s and 40s can add tens of thousands of pounds to the retirement savings they have in later life.

The default system is unlikely to give most scheme members the income they want in retirement. The minimum contribution levels of 8% of earnings will be too low for most people. Investment in a default fund which is likely to be managed on a fairly cautious basis, sacrificing higher eventual returns for a less bumpy ride, means their money won't grow as fast or as high as it could. Failing to engage with potential options, because choices are already made for them, will probably leave them working longer, or stopping work with less than they had hoped.

This policy disconnect, how to help investors transition from disengagement to engagement, is the subject of this policy paper. We've written it after analysing the engagement levels of almost 60,000 active members of workplace pensions.

Crunching the numbers shows that engaging just a little, for example improving investment returns by 1% and increasing contributions by 2%, could boost the pot of someone on average earnings by £113,000 by the time they reach State Pension Age; a 62% uplift.

Our analysis shows that, far from burying their head in the sand, people are prepared to take control of their own retirement. Half are prepared to contribute more than the minimum set by their employer and 22% have chosen to invest outside the default fund. This is not just those closest to retirement, as 36% of 20-29 year olds opt to increase their pension contributions. In fact, 73% of pension members are engaging with their retirement planning, based on 7 factors varying from setting up online access to increasing their contribution level.

Engaging people should get easier. Our trends show that pensions get more interesting the larger people's pots grow. Only half of people engage with a pension pot under £5,000 but that jumps to three quarters with a pension of £5,000-£10,000. Changes to auto-enrolment rules in the short term, and those planned for the next decade, could see the waiting time for someone with average earnings, to get a pension of more than £5,000, fall from nine years to just three.

But there are challenges. Our analysis also shows where engagement can be trickier. Women in particular tend to lack confidence when it comes to choosing investments. Multiple rule changes for higher earners appear to be causing disengagement, as engagement wanes amongst people earning over £100,000. An interesting quirk also shows younger people are less likely to have online access to their pension, but more likely to log-in when they do have it.

The opportunity to drive higher levels of engagement brings opportunities to future UK pension policy:

- The government may not need to drive minimum contributions higher. We know 8% is not enough, but engagement is possible and people will actively contribute more anyway. The DWP could instead look to focus on insisting employers have a matching structure to incentivise further employee contributions. That way employers are only paying out for those members who actually want to pay more themselves.
- Both the FCA and the Pension Regulator should make engagement a fundamental measure of the quality of workplace pension schemes.
- The increase in engagement levels when pots get larger should be helped with the introduction of the Pension Dashboard and is a reason to continue with this tech project.
- The potential of the midlife MOT is huge, given the importance of human interaction. Driving engagement higher in the early years of a career will ensure demand for this kind of service exists when midlife arrives.

Ultimately, engagement is not necessarily about the range of different tools and calculators used by pension providers, it's about getting results that change the financial future for pension savers.

WHERE NOW, AND WHERE NEXT?
The world of pensions is unlikely to be described as high octane, but has been on a bit of a roller coaster ride lately. The Brexit induced pause into any rule tweaks and policy changes, allows us some time to reflect on what more needs to be done.

Auto-enrolment has gone a long way to solving the problem of getting people saving, although there is still work to do with the part-time workers and the self-employed.

The combined forces of the retail distribution review, workplace pension charge cap and increased scrutiny from Independent Governance Committees have driven out some of the high costs from older style pension policies. Pension investors can now be a lot more confident about enjoying value for money.

New flexible retirement rules have proved exceedingly popular with savers and these new rules look destined to be better suited to the longer, more fluid transition into retirement that many of us will need.

So we have more people saving into competitively priced, modern day pensions. Retirement rules are fit for our more flexible working patterns, yet still something is missing. Inertia has been the saviour of pensions, but it now needs to work alongside engagement to provide a truly world-class pension system. This is currently conspicuous by its absence.

WHY ENGAGE?
Put simply, engagement can deliver better saving habits, more confident financial decision-making and bigger pension pots at retirement. When we cut through everything else, what really matters is having a large enough pension pot at retirement to deliver sufficient income, and provide flexibility so you can leave the working world on your own terms.

The two biggest factors that impact on the size of your pension pot at retirement are the investment returns, and the amount you pay in. The fate of two pension savers with identical earnings but different levels of engagement tells its own story.

ENGAGED ERICA
£295,000 pension at age 68

Erica is enrolled into her pension at age 22, but immediately decides to increase her contributions to 10% of salary and chooses to invest slightly more adventurously because she recognises she has time on her side. Her pension pot grows by 6% every year.

She also registers immediately for online access and logs in at least once every year to check on how her retirement savings are growing. This regular habit means she always knows the value of her plan and there are no nasty surprises when she starts to consider working less as she gets older. It also meant that she took up a mid-life review of her retirement plans when her employer offered.

Erica sets up a nomination to ensure the Trustees know who she would like the money to be passed to if she were to die. She changes the nomination several times as her circumstances change.

Erica has a pension big enough to provide sufficient income and she is also able to retire before State Pension Age if she wants.

DISENGAGED DYLAN
£181,000 pension pot at age 68

Dylan is enrolled into his pension at age 22. Retirement is so far away and it seems so complicated, he is really just grateful that he has got started. He contributes 8% of salary and his investments grow by 5% every year.

Dylan occasionally used to get statements from his pension provider in the post, although they normally found their way into the bin. In fact, he cannot remember having received a statement for a few years, he is not sure that they even have his new address.

Around the age of 60, some of Dylan's friends start to talk about their pensions. He knows he has always been a member of a pension so assumes he will be OK. Around 6 months from retirement he contacts his pension providers. He gets quite a shock when he realises his pension probably won't provide him with the kind of income he needs to live on. He ends up working for a lot longer than friends his age.

MEASURING ENGAGEMENT – FOCUS ON RESULTS

Measuring the results of engagement is crucial as it reflects the actual experience of the member. Governance bodies can fall into the trap of looking at the tools that are available to members without going on to analyse the impact they have on member engagement.

What matters most for pension members is that their pot is large enough to provide flexibility and sufficient income for their retirement. Pension schemes must focus on how they can help members improve their financial future and ensure they do not sleepwalk into retirement.

It's crucial to help people make confident choices about their pension. Hargreaves Lansdown looks after three broad types of pension investor.

- People who seek us out unprompted and are happy to manage their own investments
- People we give regulated financial advice
- People who save for retirement with Hargreaves Lansdown because their employer has a workplace pension with us.

Confidence levels for those in workplace pensions are understandably lower, and it's this group that we have focused on for our analysis.

> “What matters most for pension members is that their pot is large enough to provide flexibility and sufficient income for their retirement.”

HARGREAVES LANSDOWN'S FINANCIAL ENGAGEMENT DASHBOARD

We've built a Financial Engagement Dashboard to monitor the actions people take with their workplace pension. It works by looking at seven different choices that pension members can make to put them on track for a better retirement - working out how many of those choices each member has made.

WHAT ARE THESE SEVEN CHOICES?

- **Contributions** – electing to pay more than the minimum level set by their employer.
- **Investment Choice** – changing where their pension is invested.
- **Pension Transfer In** – choosing to transfer old pension schemes into their workplace plan.
- **Additional Account** – opting to save and invest alongside their pension, often for goals that are closer than finishing work.
- **Online Access** – registering to view their pension on-line.
- **Log In – Last 12 Months** – logging into their on-line account to view their pension in the last 12 months.
- **Death Benefit** – nominating who they'd like to receive their pension pot if they die.

WHY ARE THEY IMPORTANT?

We've chosen to monitor these seven behaviours for different reasons, but because they can all impact positively on the value someone enjoys from their pension. Paying in more or boosting investment returns have the biggest influence on the size of your pension pot.

Registering for online access and logging in ensures people are not heading like zombies into retirement. We also monitor those who've transferred pensions in because this allows people to be in better control of their retirement planning. Nominating a death beneficiary is incredibly important as it gives individual control on where the monies go - far better than leaving it to the pension Trustees to decide for you without any guidance.

Finally, we also monitor who's investing alongside their pension. This will not be right for everyone but there are often shorter term financial goals and understanding if these are used and who's using them is valuable.

THE RESULTS

Identifying how people engage with these choices is important to see how to improve engagement levels.

Because it's most important to contribute more and improve investment returns, let's focus on these two to start with.

Half of people choose to pay more than the minimum contribution level set by their employer, whilst 22% have gained the confidence to make their own investment decisions. In separate work, we've identified that those making their own investment choices are making a good fist of it. The average return of the 10 most popular funds chosen by the engaged investors has beaten the returns of the average default fund by 4.89% every year for the past 5 years.

The reason for this remarkable outperformance is these pension members are generally prepared to take more risk than a default fund investment and they use some of the best active fund managers available. While we can't expect this level of outperformance to continue throughout the lifetime of a saver, it shows it's possible to influence your financial future.

Itemised engagement – a breakdown of the seven choices

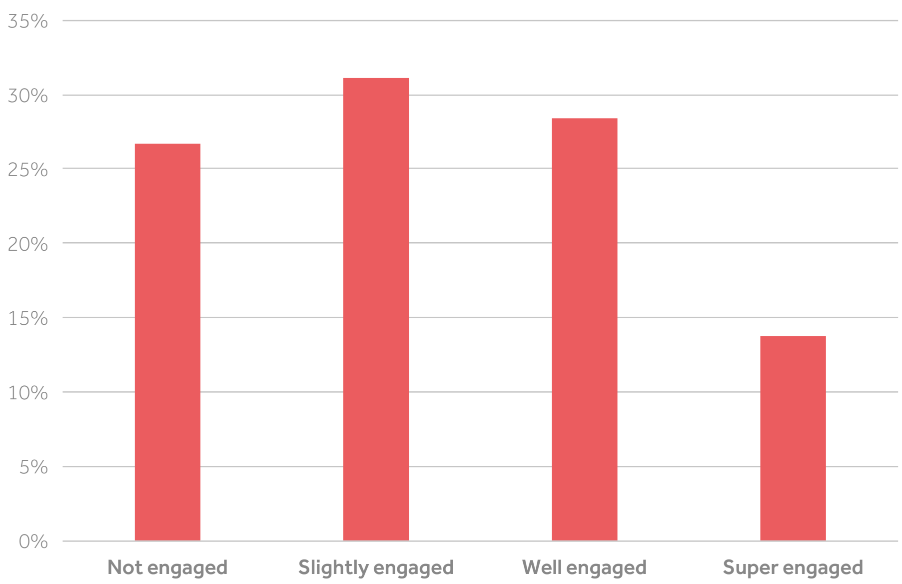
ENGAGEMENT

Contributions	Investment Choice	Pension Transfer In	Additional Account	Online Access	Log In – Last 12 Months	Death Benefit
Paying more than the minimum	Made an investment outside of the default	Transferred in another pension	Saving into an additional account with HL	Registered to view account online	Logged in to view account – last 12 months	Set up a nominated beneficiary
50% paying more than the minimum	**22%** making own decisions	**23%** transferred in another pension	**12%** with additional account	**59%** have online access	**77%** with online access logged in	**20%** have nominated beneficiary

Looking at the results in isolation is interesting, but stitching these results together provides a richer insight into the engagement of workplace pension members. The seven metrics on the dashboard allow us to assign every workplace pension member a score of 0-7 based on how engaged they are. A score of zero means they've engaged with none of the factors at all. Someone who's decided to up their contributions, register for online access and log-in within the last 12 months would have a score of 3.

From this we can identify that 73% of members are engaging with their workplace pension. More than 4 in 10 members are engaging well with their pension (this denotes an engagement score of 3 or more).

PENSION ENGAGEMENT



Note: not engaged is a score of 0, slightly engaged is a score of 1 or 2, well engaged is a score of 3 or 4 and super engaged requires a score of 5, 6 or 7.

IDENTIFYING TRENDS

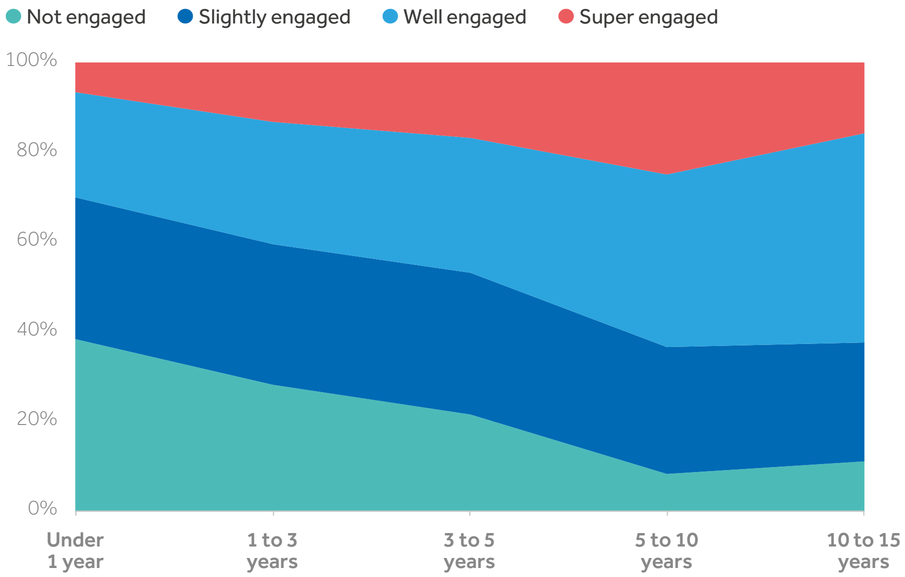
Once each member is given an engagement score it's possible to identify overall trends, as well as more localised ones.

Three factors stand out that influence overall engagement.

1. Engagement increases with the time you have been paying into a workplace pension.

People do not instantly become savvy pension savers, they need regular communications to build confidence and improve understanding over time. We also attribute this trend to a growing familiarity with the service being offered. An equivalent, non-pension related example, is how we use our mobile phones. As time goes by, we become more familiar with our handset and have more confidence using it. A change of mobile provider or upgrade to the latest handset can leave you wallowing in uncertainty.

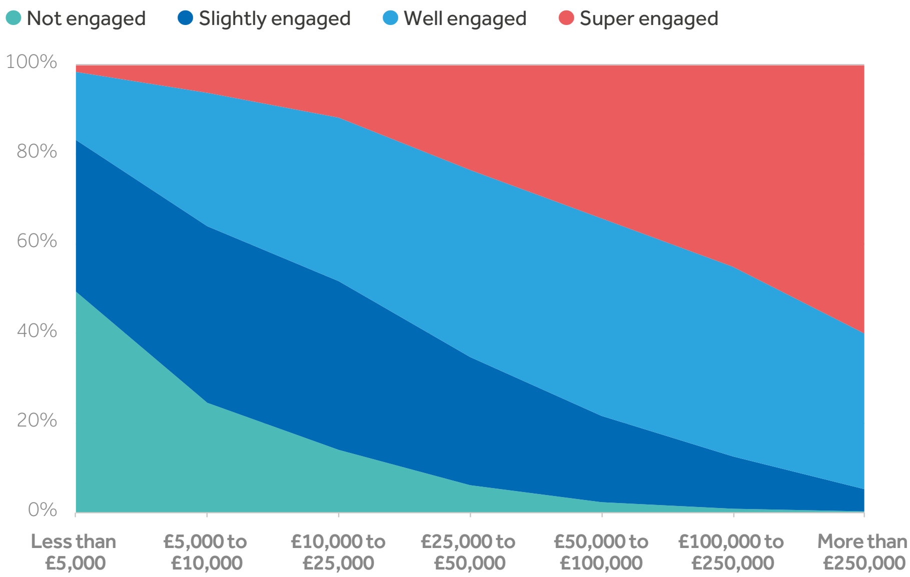
ENGAGEMENT LEVELS BY TIME CONTRIBUTING



2. People tend to be more engaged with their pension as it increases in value.

This is a well-known phenomenon, originally from research in Australia. Although it's possible to improve engagement in people with smaller pots as 50% with a pension under £5,000 are engaging. The engagement levels ramp up quite quickly, with 76% engaging when they have a pot of between £5,000 and £10,000. The pension world should be optimistic. At the moment, auto-enrolment means many people still only have small amounts set aside in their pensions. As contributions increase we should also see an uplift in the appetite to engage. This also means that consolidating pensions, and the Pension Dashboard, are crucial to driving higher levels of engagement.

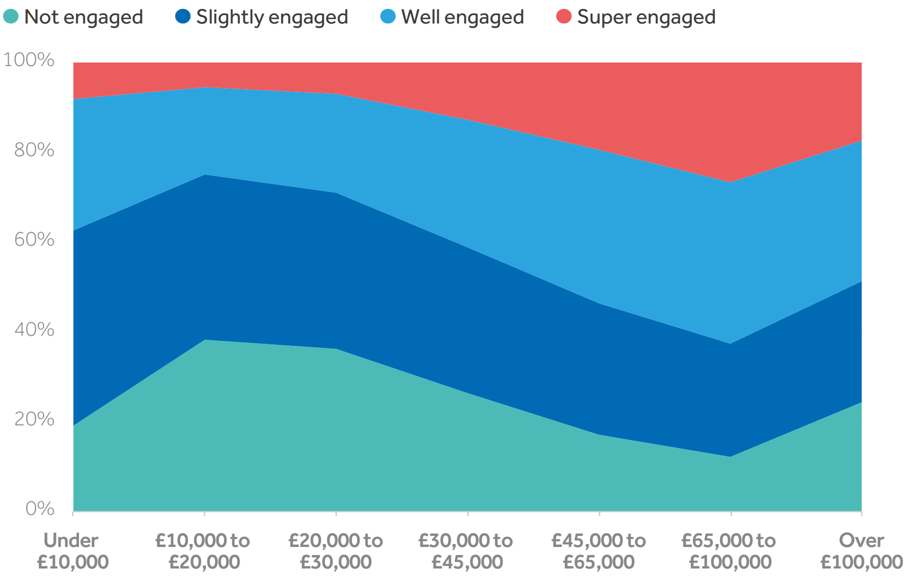
ENGAGEMENT LEVELS BY PENSION POT SIZE



3. Engagement dwindles among the highest earners.

Salary has an interesting influence on engagement levels. Engagement is relatively high with people earning under £10,000, but goes down to its lowest level when earnings are £10,000-£20,000. Engagement progressively improves the more you earn but falls away again when earnings go above £100,000. At first glance this appears odd, but there is an explanation. Those earning under £10,000 are often not auto-enrolled into the pension, instead needing to opt in themselves, so they need to be more engaged. As for highest earners, we think this is simply that constant rule tweaking (for example Lifetime Allowance and Tapered Annual Allowance changes) have been a huge turn off.

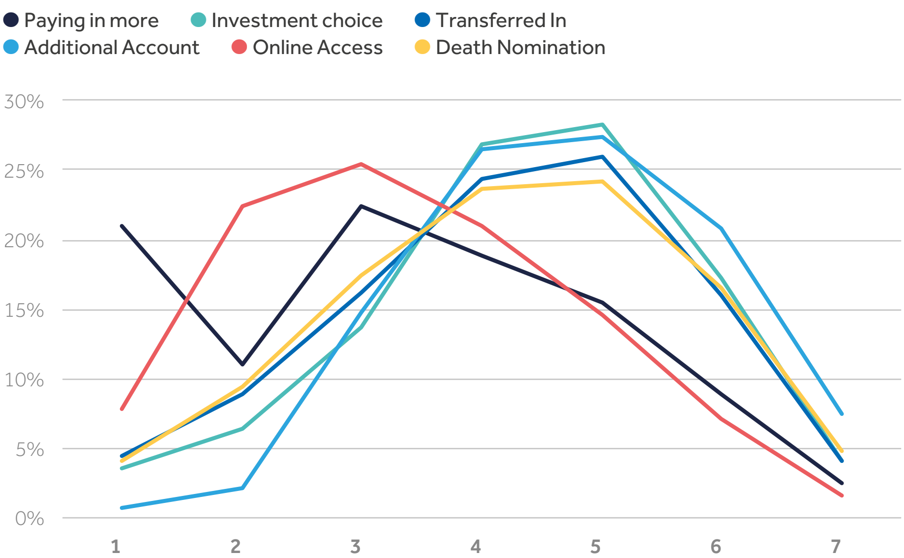
ENGAGEMENT LEVELS BY SALARY



Richer engagement

We're able to identify which behaviours lead to further engagement. For example, 21% of people who make a contribution increase do not go on to engage any further. Where people choose investments they tend to be more confident making further decisions, showing that helping people understand where their money is invested can reap more engagement rewards.

CHOICE MADE AND TOTAL ENGAGEMENT SCORE



DIFFERENCES IN THE WORKFORCE

Pulling apart the data allows us to look at the different behaviour of people in the workforce. We've specifically looked at the differences between men and women, and older and younger members.

Men and women

There's little difference in the overall engagement level; 76% of men engage, compared to 70% of women. There's also little evidence of a gender engagement gap when it comes to increasing contributions, consolidating old pensions or nominating a beneficiary. However, it's widely recognised that women are not as confident with investing as men, and this shows in our data. Not only are women less likely to choose their own investments, they're also less likely to take out an additional investment account like a Stocks & Shares ISA. There's also a digital discrepancy, with men more likely to register online and log-in than women.

	FEMALE	MALE
Overall	70%	76%
Contributions	49%	51%
Investment Choice	16%	26%
Pension Transfer In	21%	24%
Additional Account	7%	16%
Online Access	53%	63%
Log In – Last 12 Months	69%	81%
Death Benefit	18%	20%

Older and younger workers

The engagement gap between older and younger workers is significant, as might be expected. One of the challenges often cited when driving higher engagement in younger workers is that retirement is such a long way off that they struggle to identify with their distant future self.

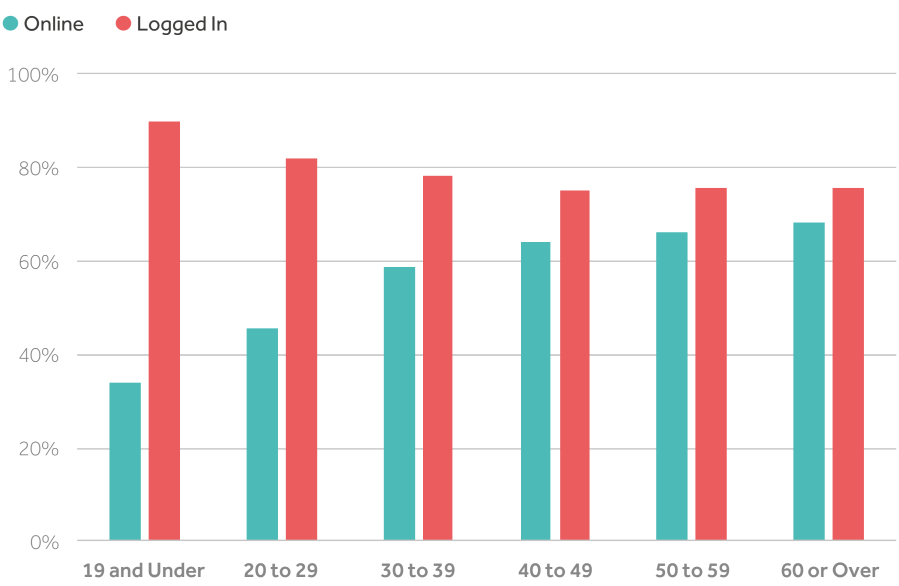
Our research shows that it's possible to engage younger workers, as 59% have taken some positive action with their pension. The numbers for older workers is far higher at 81%.

	UNDER 30	50 PLUS
Overall	59%	81%
Contributions	36%	61%
Investment Choice	14%	23%
Pension Transfer In	10%	28%
Additional Account	9%	14%
Online Access	45%	67%
Log In – Last 12 Months	82%	75%
Death Benefit	7%	30%

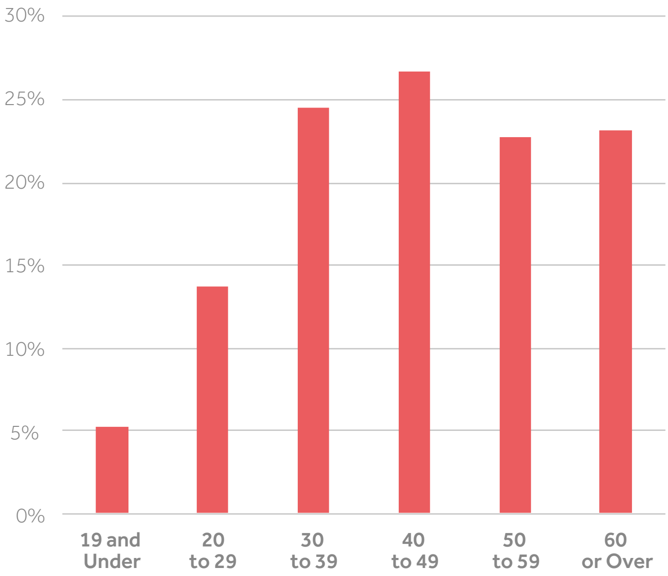
The over 50s show higher levels of engagement than the under 30s across all the measures, with the exception of the logging in rate. The digital engagement story is interesting: the older you are, the more likely you are to have online access, but you are less likely to log in.

Note: This shows the proportion of all members who have registered for online access, but the proportion logging in is based solely on the population who have actually registered for online access.

DIGITAL ENGAGEMENT BY AGE

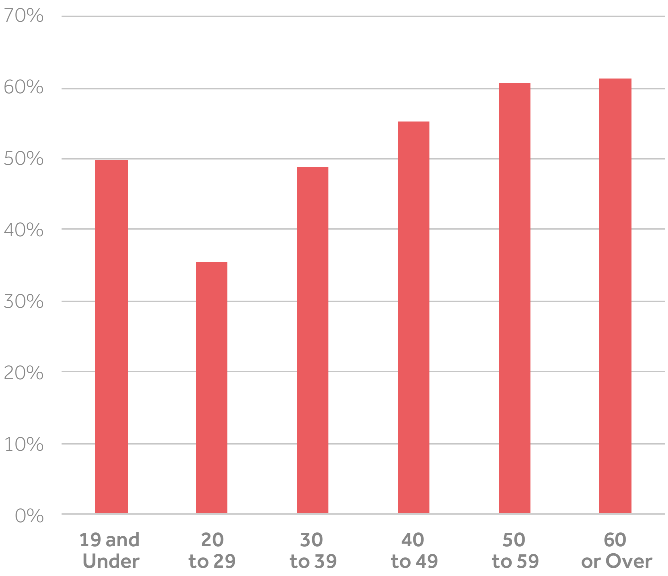


CHOOSING INVESTMENTS BY AGE



Age 30 seems to be a watershed moment for having the confidence to make investment choices with your pension, with a significant step up in activity.

INCREASING CONTRIBUTIONS BY AGE



Young people are often accused of not being prepared to save into a pension, but we've found that 36% of those under 30 are happy to increase the amount they pay in.

NON-ENGAGEMENT IS NOT NECESSARILY BAD

We must be clear, not engaging with particular metrics is not necessarily a bad thing. Examples of this include:

1. Someone is helped to understand where their default fund invests. With this knowledge, they confidently decide that this one-size-fits-all investment actually suits them. This is a great outcome for the member, but would not show up in the engagement scores.

2. Someone may have weighed up whether or not to pay more into their pension, but after running through their household budget decided boosting their contributions is not the right thing to do now.

3. Some people may not have short term investment goals, so saving into a pension is all they are looking to do.

"The value of face-to-face contact when engaging pension members is particularly important. More than three out of 10 members we analysed has had a face-to-face meeting."

DRIVING THIS ENGAGEMENT

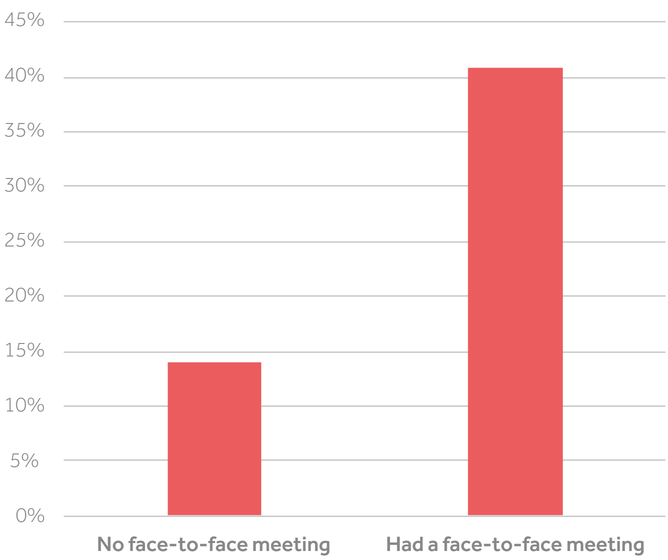
Building confidence in pension members takes time, with regular communications in the post, online, by e-mail and face-to-face. To do this properly takes careful planning, considered content, collaboration between employer and provider, and plenty of resources.

The value of face-to-face contact when engaging pension members is particularly important. More than three out of 10 members we analysed has had a face-to-face meeting. Personal engagement has an interesting impact on contributions and investment choices.

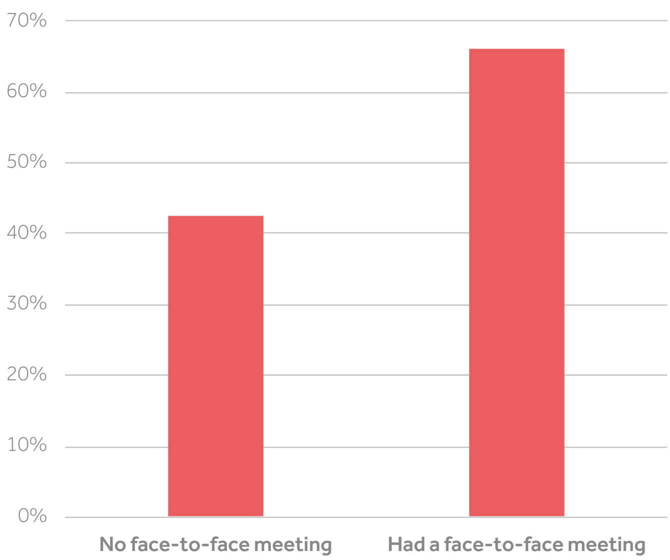
Both see improved engagement where there's a face-to-face meeting, but those confident enough to choose their own investment triples when a meeting has been provided. Often people have heard of the stock market, but don't understand their options and this help clearly builds enough confidence for people to make choices that impact on their financial future.

The benefits of face-to-face engagement add weight to the Government's Midlife MOT initiative, where people have the opportunity to assess what the end of their working life and their transition from retirement might look like.

CHOOSING INVESTMENTS BY FACE-TO-FACE



INCREASING CONTRIBUTIONS BY FACE-TO-FACE



WHERE NEXT

Where does all this insight leave us?
There's already plenty of work in train that can help drive engagement higher.

AUTO-ENROLMENT

The twin changes to the auto-enrolment rules from the mid-2020s will bring people into the pension system from 18 and also deliver contributions from the first £1 earned. That change alone could deliver a boost in pension pot size of around £40,000 by retirement age (a 21% uplift).

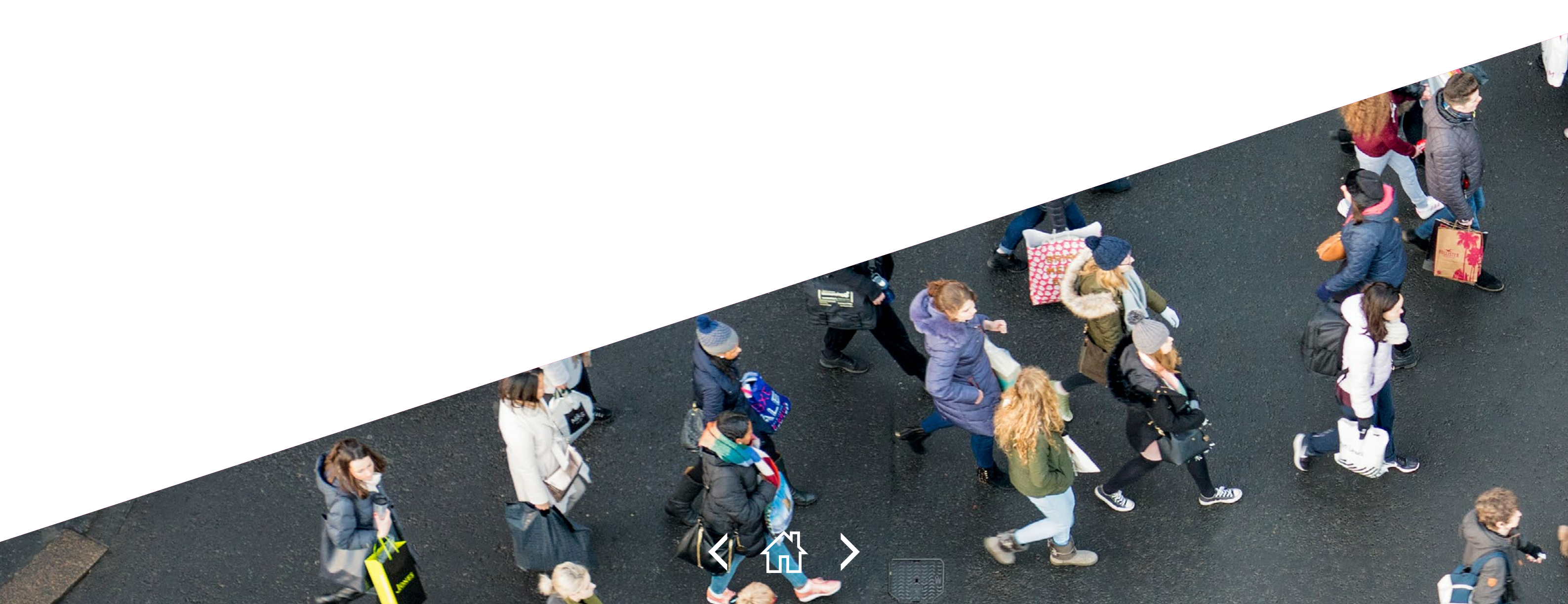
From an engagement point of view, it also means someone on average earnings could have a pension pot of more than £5,000 after 3 years as opposed to under the first stage where it would take around 9 years. Given how important pot size is to engagement there must be room for optimism.

We also question the assumption that minimum contributions should increase. We don't disagree that people should pay more, but we could rely on people taking responsibility to do it themselves. The DWP could consider changes to insist employers offer a contribution incentive on top of the minimum levels. Given half of members have taken action to pay more in, this could be a more pragmatic – and empowering – solution than forcing employers to automatically pay more.

PUTTING MEMBERS IN CONTROL OF THEIR OWN PENSION

A further change to the auto-enrolment rules could help to transform individuals' engagement with their retirement saving. At present, when someone changes jobs, they're forced to suspend their existing pension and to join their new employer's scheme in order to benefit from their employer's pension contributions. This disruption to their savings activity undermines any engagement they've already established. Just imagine how difficult it would make people's lives if they were forced to change bank accounts every time they switched jobs; yet this is pretty much what we do with their pension.

The auto-enrolment rules should be modified so that, when someone changes jobs and they already have a pension they're happy with, they should be allowed to ask their new employer to make contributions to their existing pension. This change to the system could be achieved with only a modest change to the auto-enrolment rules and with minimal disruption to employers.



BANISH THE ONE-TRICK PONY

The pension industry has become very good at talking about how people should pay more in, but have shied away from helping people make confident investment decisions. Both have a significant impact on the size of your pension, yet the investment side is largely ignored. It's true that it's harder to engage, but the industry should rise to the challenge. There's nothing more likely to turn people off saving than by keep telling them they have to pay more.

MIDLIFE MOT

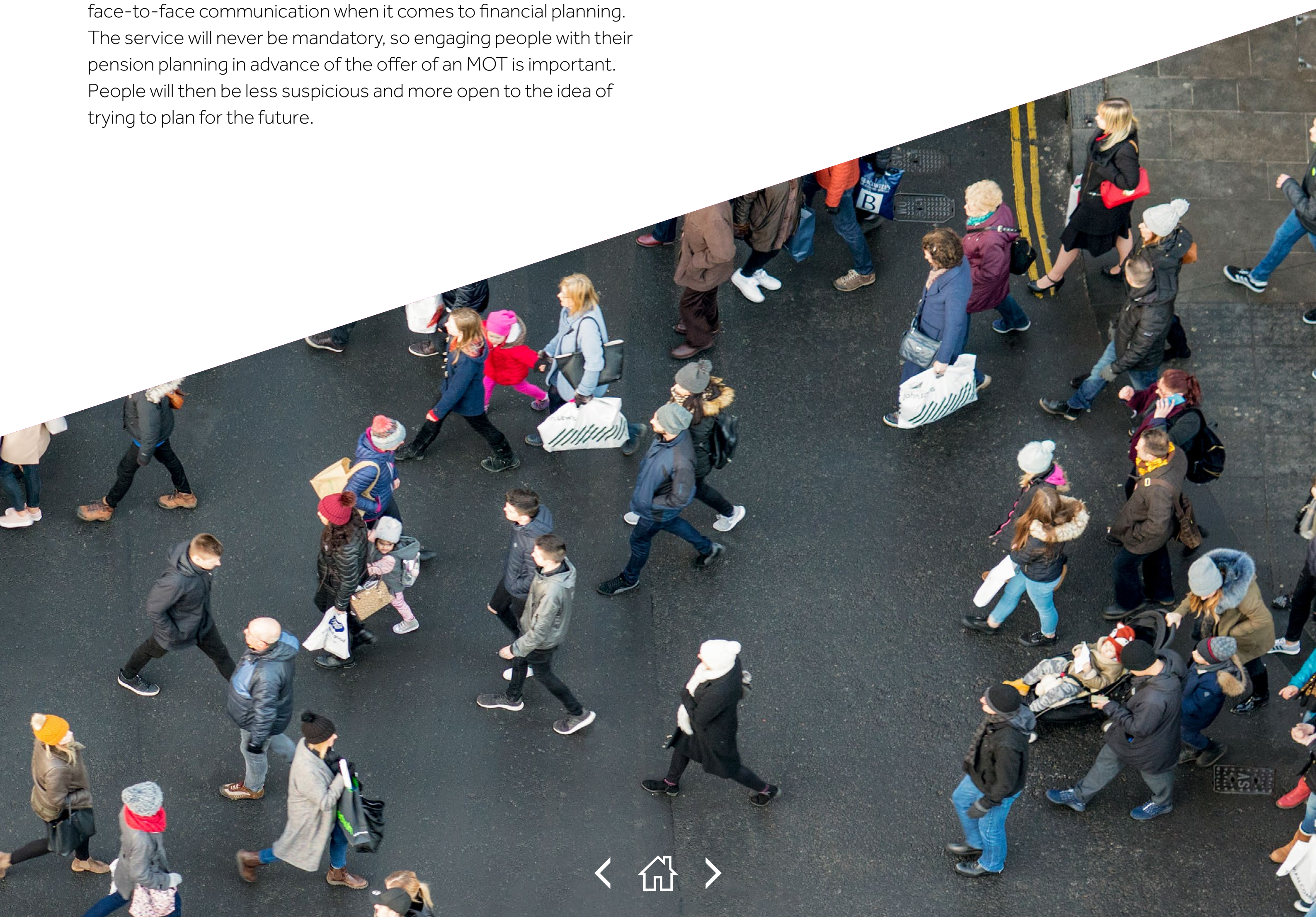
The midlife MOT has the potential to be a game changing initiative, helping people understand and take control of their final decade or two at work. Our analysis shows the immense value of face-to-face communication when it comes to financial planning. The service will never be mandatory, so engaging people with their pension planning in advance of the offer of an MOT is important. People will then be less suspicious and more open to the idea of trying to plan for the future.

THE ROLE OF THE REGULATORS

The Pension Regulator and the FCA should both make member engagement a core test of the quality and value of a pension scheme. It's imperative that this core test is not about measuring the number of tools and calculators offered, but is about monitoring the levels of engagement that will, in turn, drive bigger pension pots for members.

METHODOLOGY

Our analysis has looked at the behaviour of over 58,000 active members of the Hargreaves Lansdown Workplace Pension.



ABOUT US

We're Hargreaves Lansdown – a secure, FTSE 100 company helping UK savers and investors for 35 years. Over one million people already trust us to help them save and invest with confidence.

We make it easy for you to manage your pension online with our mobile and tablet apps. Our Helpdesk is here six days a week to help, including evenings:

- Monday - Thursday 8am to 7pm
- Friday 8am to 6pm
- Saturday 9:30am to 12:30pm

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